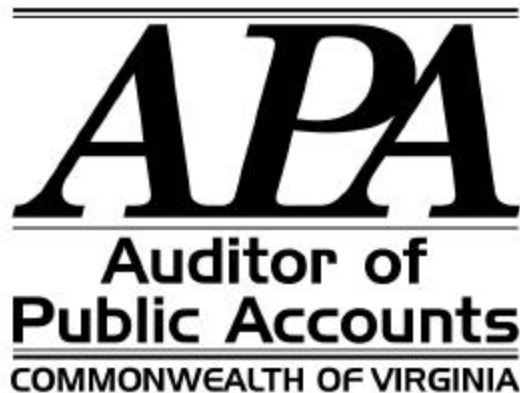


**DEPARTMENT OF ENVIRONMENTAL QUALITY
RICHMOND, VIRGINIA**

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2003**



AUDIT SUMMARY

Our audit of the Department of Environmental Quality for the year ended June 30, 2003, found:

- internal control matters that we consider reportable conditions, but we do not consider these to be material weaknesses;
- proper recording and reporting of transactions, in all material respects, in the Commonwealth Accounting and Reporting System; and
- no instances of noncompliance with applicable laws and regulations tested that are required to be reported under Government Auditing Standards.

Our findings are discussed in the section entitled “Internal Control Findings and Recommendations.”

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SELECTED AGENCY INFORMATION

General Overview

The Department of Environmental Quality (the Department) protects the Commonwealth's natural resources by administering state and federal environmental programs, issuing permits, monitoring water and air quality, and inspecting waste facilities. The Department conducts extensive monitoring to ensure compliance with state and federal standards for water quality, air quality, and waste management. The Department also enforces regulations promulgated by the State Water Control Board, the Board of Waste Management, and the Air Pollution Control Board.

The Department operates through its central office, seven regional offices, and four satellite and specialized offices. The following chart illustrates the Department's funding sources and spending levels for fiscal year 2003.

<u>Revenues:</u>	<u>2003</u>
General fund appropriations	\$ 32,156,120
Capitalization grants	13,794,537
Other federal grants	16,445,317
Taxes and fees	42,882,603
Permits fees	12,394,310
Other sources	<u>10,645,221</u>
Total revenues	<u>\$ 128,318,108</u>
<u>Expenses and loan disbursements:</u>	
Response and remediation	\$ 38,652,630
Technical and financial assistance	30,428,341
Resource management	27,904,624
Administration and support	17,697,974
Monitoring and evaluation	7,867,425
Other	<u>6,709,421</u>
Total expenses	<u>\$ 129,260,415</u>

Tax revenues represent funds collected by other agencies and transferred to the Department for activities such as litter control, petroleum tax, vehicle emissions inspection, and waste tire disposal. Other sources of revenues include recovery of indirect costs, civil penalties and charges, interest, and miscellaneous revenue. Other program expenses include research and planning, policy and program development, and information and education assistance.

Virginia Water Quality Improvement Fund

The Commonwealth established a special permanent fund to finance the nutrient reduction strategies for the Chesapeake Bay and its tributaries, known as the "Virginia Water Quality Improvement Fund." The Department assists local governments, businesses, and individuals in reducing point source nutrient loads to

the Chesapeake Bay with technical and financial assistance made available through grants provided from the fund.

The program's primary funding source consists of ten percent of the annual Statewide General Fund revenue collections that exceed the official estimates in the General Appropriation Act and ten percent of any unreserved Statewide General Fund balance at the close of each fiscal year not mandated for reappropriation.

This fund has financed 26 point source programs, 19 of these projects are completed. The remaining projects have scheduled completion dates by the end of fiscal year 2005. To date, the Department has obligated approximately \$98.8 million through signed grant agreements, while only \$92.8 in funding is available through appropriations and interest earned. The Commonwealth has made no additional appropriations to the fund since fiscal year 2001. Without future funding the Department estimates a shortfall of approximately \$6 million for current grant obligations.

In fiscal year 2003, the Department placed emphasis on closing out five projects with relatively small balances to minimize fiscal strain. Aside from these five projects, all fiscal year 2003 reimbursements were prorated to pay 55 percent of the eligible costs and 45 percent of the costs were deferred until additional funds become available. Due to lack of appropriations, the Department has been unable to solicit any new, cooperative point source projects since fiscal year 2000. Further solicitation for projects cannot occur until State financial resources are available. If additional appropriations are not made to the fund, it is projected that the fund will not have sufficient resources to cover any reimbursements beyond amounts deferred in FY 2003 and proposed for payment in January 2004.

Title V Air Permitting Program

Title V of the Clean Air Act requires that each state develop a self-supporting operating permit program to apply state and federal requirements to stationary air pollution sources. The Department does this through their Air Permitting Program. The Department assesses fees based on the amount of pollutants released into the air and performs the Title V permit program fee calculations annually using the Consumer Price Index. In fiscal year 2003, Title V revenue and expenses totaled \$9,955,933 and \$10,275,637 respectively. The Program's accumulated fund balance absorbed the deficiency in revenues collected. The fund balance at June 30, 2003, was \$10,498,118.

The Virginia Petroleum Storage Tank Fund

The Virginia Petroleum Storage Tank Fund reimburses approved clean-up costs and some third party damages resulting from petroleum releases from storage tanks. The primary revenue for the Fund comes from a \$.006 per gallon fee on regulated petroleum products sold in Virginia. Regulated products include gasoline, aviation motor fuel, diesel fuel, kerosene, and heating oil. In fiscal year 2003, Virginia Petroleum Storage Tank Fund revenue and expenses totaled \$36,122,594 and \$36,359,506, respectively.

INTERNAL CONTROL FINDINGS AND RECOMMENDATIONS

Monitor Access to Statewide Systems

The Department is a summary user of the Commonwealth Accounting and Reporting System (CARS); therefore, CARS access is only required for a limited number of individuals. We found that multiple agency personnel, whose job responsibilities do not require the use of CARS, currently have CARS access. Access control is vital to ensure the integrity of information submitted to statewide systems. Allowing agency personnel to have unnecessary access increases the risk of unauthorized changes and misuse of the systems.

The Department should remove systems access for agency personnel that do not require use, and in the future, closely monitor access to statewide systems. A quarterly review of individuals who have access to statewide systems will strengthen controls over systems access.

Implement Information Technology Security Policies and Procedures

In December 2001, the Department of Technology Planning issued the Information Technology Security Standard. This standard is applicable to all State agencies that manage, develop, purchase, and use information technology resources in the Commonwealth. The purpose of this standard is to define the minimum requirements for the administration of an agency's information technology security program and to promote secure communications and the appropriate protection of information resources within the Commonwealth.

We found the Department is not in compliance with the Information Security Standard. The Department does not currently have a business impact analysis nor have they conducted an agency-wide risk assessment or established a business continuity plan. This noncompliance increases the probability that safeguards over critical agency operations and information are inadequate to protect the confidentiality, integrity, and availability of data, information, and systems.

The Department should follow the Commonwealth's Security Architecture in order to comply with the Information Technology Security Standard. The Department has taken steps to begin the development of these plans, and we encourage them to continue their efforts and to ensure that appropriate resources are available as needed to complete the process.



Commonwealth of Virginia

Walter J. Kucharski, Auditor

Auditor of Public Accounts
P.O. Box 1295
Richmond, Virginia 23218

February 11, 2004

The Honorable Mark R. Warner
Governor of Virginia
State Capitol
Richmond, Virginia

The Honorable Lacey E. Putney
Vice Chairman, Joint Legislative Audit
and Review Commission
General Assembly Building
Richmond, Virginia

INDEPENDENT AUDITOR'S REPORT

We have audited the financial records and operations of the **Department of Environmental Quality** for the year ended June 30, 2003. We conducted our audit in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

Audit Objective, Scope, and Methodology

Our audit's primary objectives were to evaluate the accuracy of recording financial transactions on the Commonwealth Accounting and Reporting System, review the adequacy of the Department's internal control, and test compliance with applicable laws and regulations.

Our audit procedures included inquiries of appropriate personnel, inspection of documents and records, and observation of the Department's operations. We also tested transactions and performed such other auditing procedures, as we considered necessary to achieve our objectives. We reviewed the overall internal accounting controls, including controls for administering compliance with applicable laws and regulations. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances.

Revenues	Fixed Assets
Expenditures	

We obtained an understanding of the relevant internal control components sufficient to plan the audit. We considered materiality and control risk in determining the nature and extent of our audit procedures. We performed audit tests to determine whether the Department's controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations.

The Department's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

Our audit was more limited than would be necessary to provide assurance on internal control or to provide an opinion on overall compliance with laws and regulations. Because of inherent limitations in internal control, errors, irregularities, or noncompliance may nevertheless occur and not be detected. Also, projecting the evaluation of internal control to future periods is subject to the risk that the controls may become inadequate because of changes in conditions or that the effectiveness of the design and operation of controls may deteriorate.

Audit Conclusions

We found that the Department properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System. The Department records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System.

We noted certain matters involving internal control and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgment, could adversely affect the Department's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial records. Reportable condition entitled "Monitor Access to Statewide Systems" and "Implement Information Technology Security Policies and Procedures," are described in the section titled "Internal Control Findings and Recommendations." We believe that none of the reportable conditions is a material weakness.

The results of our tests of compliance with applicable laws and regulations disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

EXIT CONFERENCE

We discussed this report with management at an exit conference held on February 26, 2004.

AUDITOR OF PUBLIC ACCOUNTS

NJG:whb
whb:45



COMMONWEALTH of VIRGINIA

DEPARTMENT OF ENVIRONMENTAL QUALITY

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W. Tayloe Murphy, Jr.
Secretary of Natural Resources

Robert G. Burnley
Director

(804) 698-4000
1-800-592-5482

March 1, 2004

Mr. Walter J. Kucharski
Auditor of Public Accounts
P. O. Box 1295
Richmond, VA 23218

Dear Mr. Kucharski:

The Department of Environmental Quality has reviewed your audit report of the Department of Environmental Quality for the period ended June 30, 2003. The audit summary found:

- internal control matters that were considered reportable conditions, but were not considered material weaknesses;
- proper recording and reporting of transactions, in all material respects, in the Commonwealth Accounting and Reporting System; and
- no instances of noncompliance with applicable laws and regulations tested that are required to be reported under Government Auditing Standards.

The internal control matters were as follows:

Internal Control Finding #1 Monitor Access to Statewide Systems

The Department is a summary user of the Commonwealth Accounting and Reporting System (CARS); therefore, CARS access is only required for a limited number of individuals. We found that multiple agency personnel, whose job responsibilities do not require the use of CARS, currently have CARS access. Access control is vital to ensure the integrity of information submitted to statewide systems. Allowing agency personnel to have unnecessary access increases the risk of unauthorized changes and misuse of the systems.

The Department should remove systems access for agency personnel that do not require use, and in the future, closely monitor access to statewide systems. A quarterly review of individuals who have access to statewide systems will strengthen controls over systems access.

DEQ Management response:

DEQ utilizes the agency-based financial system Oracle for the managing and reporting of financial transactions that ultimately are recorded in the Commonwealth's centralized general ledger system (CARS). Prior to the implementation of Oracle, DEQ processed all financial transactions directly to CARS. Until recently, residual processes that continued to require direct input to CARS included Interagency Transactions (IAT's) and temporary travel advances. CARS data entry will continue to be required for the DEQ payroll staff to key health care Interagency Agency Transactions. Access to CARS for inquiry purposes will also continue for appropriation and check data.

DEQ will review the active listing for CARS data entry and approval access and delete as many users as possible in light of current job responsibilities. We will also develop an agency policy that will outline CARS access procedures.

Internal Control Finding #2 Implement Information Technology Security Policies and Procedures

In December 2001, the Department of Technology Planning issued the Information Technology Security Standard. This standard is applicable to all State agencies that manage, develop, purchase, and use information technology resources in the Commonwealth. The purpose of this standard is to define the minimum requirements for the administration of an agency's information technology security program and to promote secure communications and the appropriate protection of information resources within the Commonwealth.

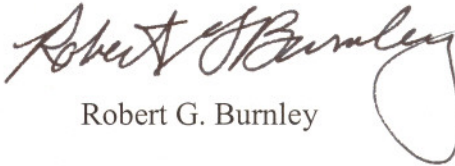
We found the Department is not in compliance with the Information Security Standard. The Department does not currently have a business impact analysis nor have they conducted an agency-wide risk assessment or established a business continuity plan. This noncompliance increases the probability that safeguards over critical agency operations and information are inadequate to protect the confidentiality, integrity, and availability of data, information, and systems.

The Department should follow the Commonwealth's Security Architecture in order to comply with the Information Technology Security Standard. The Department has taken steps to begin the development of these plans, and we encourage them to continue their efforts and to ensure that appropriate resources are available as needed to complete the process.

DEQ Management Response:

We appreciate the acknowledgement of the steps DEQ has taken to begin the development of a more robust security architecture. We have established an initial Continuity of Operations Planning (COOP) team. This team has met already to address the agency-wide risk assessment, view the existing baseline continuity plan, and begin creating milestones to deliver a written and tested continuity plan according the state mandate of June 1, 2004.

Sincerely,

A handwritten signature in dark ink, appearing to read "Robert G. Burnley". The signature is fluid and cursive, with a large loop at the end of the last name.

Robert G. Burnley

c: David VonMoll
Steven K. VonCanon

DEPARTMENT OF ENVIRONMENTAL QUALITY
Richmond, Virginia

Robert G. Burnley, Director

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